

STATE OF MICHIGAN  
IN THE SUPREME COURT

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TOMRA OF NORTH AMERICA, INC.,

Supreme Court No. 158333

Plaintiff-Appellee,

Court of Appeals Docket No. 336871  
(consolidated with Docket No. 336663)

Court of Claims Docket No. 16-000118-MT and  
Docket No. 14-000091-MT  
(consolidated with Docket No. 14-000185-MT)

v

DEPARTMENT OF TREASURY,  
STATE OF MICHIGAN

Defendant-Appellant.

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**APPELLEE'S BRIEF IN OPPOSITION TO  
APPELLANT'S APPLICATION FOR LEAVE TO APPEAL**

## TABLE OF CONTENTS

INDEX OF AUTHORITIES.....	ii
COUNTERSTATEMENT OF QUESTION PRESENTED .....	vi
I. INTRODUCTION .....	1
II. STATEMENT OF FACTS .....	3
A. Container Recycling Machines. ....	4
B. TOMRA’s Sales of Container Recycling Machines. ....	6
C. The Audit and Claims for Refund. ....	6
D. Proceedings Before the Court of Claims. ....	6
E. The Decision of the Court of Appeals. ....	7
III. STATUTES AT ISSUE .....	8
IV. STANDARD OF REVIEW .....	10
A. Interpretation and Construction of Tax Statutes.....	10
V. ARGUMENT .....	11
A. The Fundamental Principles of Statutory Interpretation Were Applied by the Court of Appeals and Review is Unnecessary. ....	11
1. Under the Plain Language of the Statute, Activities Under Subsection (3) Are Industrial Processing Activities, Irrespective of Subsection (7)(a). ....	12
2. The Court of Appeals Properly Held that the Container Recycling Machines Qualify for the Industrial Processing Exemption. ....	16
B. Failure to Perform a Non-Exempt Activity Does not Disqualify an Activity From Industrial Processing. ....	18
C. Recycling is an Industrial Processing Activity.....	22
D. The Decision has Minimal Impact. ....	23
VI. CONCLUSION.....	25

## INDEX OF AUTHORITIES

### Cases

<i>Ally Financial, Inc v State Treasurer</i> , __ Mich __; __ NW2d __ (2018) (Docket Nos. 154668, 154669 and 154670) .....	11
<i>Detroit Edison Co v Dep't of Treasury</i> , 498 Mich 28; 869 NW2d 810 (2015).....	passim
<i>DiBenedetto v West Shore Hosp</i> , 461 Mich 394; 605 NW2d 300 (2000) .....	11
<i>Elias Bros Restaurants, Inc v Dep't of Treasury</i> , 452 Mich 144; 549 NW2d 837 (1996). vi, 2, 10, 17	
<i>Evanston YMCA Camp v State Tax Comm'n</i> , 369 Mich 1; 118 NW2d 818 (1962) .....	13
<i>Ford Motor Co v Dep't of Treasury</i> , 496 Mich 382; 852 NW2d 786 (2014).....	3, 10
<i>Granger Land Dev Co v Dep't of Treasury</i> , 286 Mich App 601; 780 NW2d 611 (2009) .....	17
<i>Guardian Indus Corp v Dep't of Treasury</i> , 243 Mich App 244; 621 NW2d 450 (2000).....	10
<i>Guardian Photo, Inc v Dep't of Treasury</i> , 243 Mich App 270; 621 NW2d 233 (2000).....	11
<i>In re Dodge Bros</i> , 241 Mich 665; 217 NW 777 (1928).....	10
<i>Int'l Bus Machines v Dep't of Treasury</i> , 220 Mich App 83; 558 NW2d 456 (1996).....	10
<i>Linsell v Applied Handling, Inc</i> , 266 Mich App 1; 697 NW2d 913 (2005) .....	11
<i>Massey v Mandell</i> , 462 Mich 375; 614 NW2d 70 (2000) .....	11
<i>Mich Allied Dairy Ass'n v Auditor General</i> , 302 Mich 643; 5 NW2d 516 (1942).....	11
<i>Mich Bell Tel Co v Dep't of Treasury</i> , 229 Mich App 200; 581 NW2d 770 (1998).....	11
<i>Mich Bell Tel Co v Dep't of Treasury</i> , 445 Mich 470; 518 NW2d 808 (1994).....	13, 14
<i>Mich Milk Producers, Ass'n v Dep't of Treasury</i> , 242 Mich App 486; 618 NW2d 917 (2000) .....	11
<i>NACG Leasing v Dep't of Treasury</i> , 495 Mich 26; 843 NW2d 891 (2014).....	2, 13
<i>Sanchick v State Bd of Optometry</i> , 342 Mich 555; 70 NW2d 757 (1955).....	22
<i>State Farm Fire &amp; Cas Co v Old Republic Ins Co</i> , 466 Mich 142; 644 NW2d 715 (2002) ....	2, 14

<i>Tomra of N Am, Inc v Dep't of Treasury</i> , __ Mich App __; __ NW2d __ (2018) (Docket Nos. 336871 and 337663) .....	7, 13, 19
---	-----------

## Statutes

1999 PA 117 .....	8
2008 PA 387 .....	21
MCL 205.30(1) .....	10
MCL 205.54t.....	passim
MCL 205.54t(1)(c).....	8
MCL 205.54t(3) .....	passim
MCL 205.54t(3)(b) .....	14
MCL 205.54t(3)(c).....	14
MCL 205.54t(3)(d) .....	passim
MCL 205.54t(3)(e).....	14
MCL 205.54t(3)(f) .....	14
MCL 205.54t(3)(g) .....	vi, 1, 21
MCL 205.54t(3)(i) .....	passim
MCL 205.54t(3)(j) .....	vi, 1, 21
MCL 205.54t(3)(k) .....	vi, 1, 18, 21
MCL 205.54t(4) .....	7, 8
MCL 205.54t(4)(b) .....	17
MCL 205.54t(6) .....	18
MCL 205.54t(7)(a).....	passim
MCL 205.94o .....	1, 8, 19, 24
MCL 205.94o(1)(c).....	8
MCL 205.94o(3) .....	passim
MCL 205.94o(3)(b).....	14

MCL 205.94o(3)(c).....	14
MCL 205.94o(3)(d).....	15
MCL 205.94o(3)(e).....	14
MCL 205.94o(3)(f) .....	14
MCL 205.94o(3)(i) .....	15
MCL 205.94o(4) .....	8
MCL 205.94o(6) .....	19
MCL 205.94o(6)(b).....	17
MCL 205.94o(7)(a).....	15, 16, 17, 19
MCL 445.571 <i>et seq.</i> .....	10
MCL 445.571 to MCL 445.576 .....	20
MCL 445.653(t) .....	21

### Other Authorities

2A Singer, Sutherland Statutory Construction (7 <sup>th</sup> ed), § 47.07 .....	14
<a href="http://www.all-recycling-facts.com/glass-recycle.html">http://www.all-recycling-facts.com/glass-recycle.html</a> (accessed August 10, 2017).....	22
<a href="http://www.conserve-energy-future.com/aluminum-recycling.php">http://www.conserve-energy-future.com/aluminum-recycling.php</a> (accessed August 10, 2017) .....	22
<a href="http://www.conserve-energy-future.com/recyclingglass.php">http://www.conserve-energy-future.com/recyclingglass.php</a> (accessed August 10, 2017).....	22
<a href="http://www.conserve-energy-future.com/recyclingplastic.php">http://www.conserve-energy-future.com/recyclingplastic.php</a> (accessed August 10, 2017) .....	22
<a href="https://www.merriam-webster.com/dictionary/recycling">https://www.merriam-webster.com/dictionary/recycling</a> (accessed August 7, 2017) .....	22
Hunt, The “Just-In-Time-Method” < <a href="http://smallbusiness.chron.com/justintime-method-31185.html">http://smallbusiness.chron.com/justintime-method-31185.html</a> > (accessed March 13, 2017).....	20
Revenue Admin Bull 2000-4 .....	15, 23
Senate Legislative Analysis, SB 544, HB 4744, 4745, and 4586 (July 19, 1999).....	8

### Rules

MCR 7.305(B) .....	2
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MCR 7.305(B)(2).....	11
MCR 7.305(B)(3).....	11
MCR 7.305(B)(5).....	11

## COUNTERSTATEMENT OF QUESTION PRESENTED

The industrial processing exemption from sales tax was enacted to prevent a “pyramiding” of tax. That is, if a process results in a product that is sold, the components used or consumed in its production are not taxed so that the product is not subject to double taxation. *Elias Bros Restaurants, Inc v Dep’t of Treasury*, 452 Mich 144, 152; 549 NW2d 837 (1996). Plaintiff-Appellee sells and leases Container Recycling Machines and related parts, which test, sort, puncture, and crush recyclable beverage containers that are remanufactured into consumer products. With that background, the questions presented are:

1. Did the Court of Appeals correctly hold that Plaintiff’s Container Recycling Machines and parts are exempt under the industrial processing exemption when the Container Recycling Machines and parts perform the following functions that are statutorily defined as exempt activities:

- changing the form, composition, quality, combination, or character of the property for ultimate sale at retail (MCL 205.54t(7)(a));
- performing inspection, quality control, and testing (MCL 205.54t(3)(d));
- remanufacturing (MCL 205.54t(3)(g)),
- handling production materials (MCL 205.54t(3)(j));
- recycling activities (MCL 205.54t(3)(i)); and,
- storing in-process materials (MCL 205.54t(3)(k))?

Plaintiff-Appellee answers, “Yes.”

Defendant-Appellant answers, “No.”

The Court of Appeals answered, “Yes.”

The Court of Claims did not address this question.

## I. INTRODUCTION

The Court of Appeals decision below is a routine application of the well-established rules of statutory construction that conforms to this Court's most recent interpretation of the "industrial processing" exemption in *Detroit Edison Co v Dep't of Treasury*, 498 Mich 28; 869 NW2d 810 (2015) and is not worthy of this Court's review. The Container Recycling Machines at issue are familiar to many consumers as the machines that accept recyclable beverage containers and sort, crush and shred those containers in the first step in a mandatory beverage container redemption and recycling system in Michigan. The glass, plastic and aluminum recycled from these containers is used to produce new consumer products.

The Court of Appeals held that the Container Recycling Machines qualify for industrial processing exemption because they convert and condition tangible personal property—used beverage containers—by changing the form, composition, quality, combination, or character of the property for ultimate sale at retail (MCL 205.54t(7)(a))<sup>1</sup> and perform inspection, quality control, testing (MCL 205.54t(3)(d)), remanufacturing (MCL 205.54t(3)(g)), production material handling (MCL 205.54t(3)(j)), recycling activities (MCL 205.54t(3)(i)) and storage of in-process materials (MCL 205.54t(3)(k)) that the Legislature specifically included in the definition of qualified "industrial processing."

The Opinion below is supported by two unremarkable holdings. First, that as a matter of statutory interpretation, activities that fall under 205.54t(3) or 205.54t(7)(a) are exempt industrial processing. This is merely a repeat of this Court's holding in *Detroit Edison*, 498 Mich at 39;

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<sup>1</sup> An identical industrial processing exemption is included in the Use Tax Act at MCL 205.94o. Because the provisions of MCL 205.54t and MCL 205.94o are identical, to avoid duplication, only the references to the sales tax exemption are included, although TOMRA also seeks exemption from Use Tax under MCL 205.94o upon repair parts used in the Container Recycling Machines.



(the test is whether industrial processing is occurring is under **either** subsection (7)(a) **or** (3)). The Legislature's specific listing of activities under subsection (3) of MCL 205.54t as "included" in industrial processing is an extension of, and in addition to, the industrial processing definition in MCL 205.54t(7)(a). See also, *NACG Leasing v Dep't of Treasury*, 495 Mich 26, 31; 843 NW2d 891 (2014) ("As we have stated previously, 'including' is a term of enlargement, not limitation.")

Second, industrial processing is determined by the use to which machinery is put and not where or when the machinery is used. *Elias Bros Restaurants, Inc*, 452 Mich at 157 ("to determine whether the industrial processing exemption applies, it is necessary to consider the *activity* in which the equipment is engaged"). Non exempt activities, such as raw material storage or distribution does not disqualify exempt activities under subsection (3). *Detroit Edison*, 498 Mich at 55. The Container Recycling Machines perform exempt activities under subsection (3) and qualify for exemption. In so holding, the Court of Appeals ensured that the subsection (3) listing of the exempt industrial processing activities was not rendered meaningless. *State Farm Fire & Cas Co v Old Republic Ins Co*, 466 Mich 142, 146; 644 NW2d 715 (2002) (courts must give effect to every word, phrase and clause in a statute).

The Department of Treasury's application fails to meet any of the criteria for grounds to appeal under MCR 7.305(B). The decision below is correct and well-grounded in this Court's precedential opinions on statutory interpretation and the industrial processing exemption as discussed above. The Department's argument that, despite the clear and unambiguous language of this statute, a temporal limitation must be read into subsection (3) of the statute is contrary to the fundamental legal principles of statutory interpretation. This is particularly improper when subsection 3(d) specifically allows the qualified industrial processing activities to occur at any

time prior to finished goods storage. The language of the statute controls and prohibits insertion of language and restrictions not included by the Legislature. *Ford Motor Co v Dep't of Treasury*, 496 Mich 382, 389; 852 NW2d 786 (2014). The Department's application and requested relief conflicts with this Court's prior precedent by excluding all subsection (3) processing activities that occur prior to or do not include raw material storage.

The application of the industrial processing exemption to Container Recycling Machines impacts a small industry comprised of only the two sellers in Michigan. This issue has minimal legal impact beyond this industry. No taxpayers have had their exemption limited based upon the absence of raw material storage or finished good storage in the twenty years since the expansion of the industrial processing exemption. This issue is not recurring and confirms the unremarkable proposition that when the only activity occurring is specifically defined as exempt, the absence of a precursor non-exempt activity, such as raw material storage, does not negate the exemption. The Department's prophecy of financial doom is unsupported by the historical application of the industrial processing exemption across diverse manufacturers.

For the foregoing reasons, and as more fully explained herein, this Court should deny the Application for Leave to Appeal.

## **II. STATEMENT OF FACTS**

In Michigan, TOMRA operates in the used beverage container recycling industry. TOMRA provides products and services to facilitate the recycling of used beverage containers. Specifically, TOMRA sold and leased Container Recycling Machines and TOMRA also serviced and sold parts for Container Recycling Machines.<sup>2</sup> TOMRA did not sell any other items of

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<sup>2</sup> Appellant's Brief in Docket No. 336871, Ex 1 Riegle Aff Tab A; Ex 4 Riegle Dep at p 46.

tangible personal property in Michigan during the 2011 tax period.<sup>3</sup> TOMRA also provided service and sold maintenance contracts to its customers and, pursuant to those contracts, would repair a Container Recycling Machine if it was not working properly.<sup>4</sup>

#### **A. Container Recycling Machines.**

Container Recycling Machines are the first step in recycling aluminum, plastic, and glass containers into new aluminum, plastic, and glass containers for reuse and resale.<sup>5</sup>

Container Recycling Machines receive, sort, inspect, perform quality control, perform production material handling and are otherwise engaged in activities that constitute industrial processing activities.<sup>6</sup> During the 2011 tax period at issue, the Container Recycling Machines in Michigan accepted glass, aluminum or plastic containers, the combination of aluminum and plastic containers, or all three container types.<sup>7</sup> The machine then performs inspection, quality control and testing on the container to determine whether the container conforms to specific parameters, including whether any liquid is within the container.<sup>8</sup>

The Container Recycling Machine scans the universal product code (“UPC”) and uses the information from the UPC and information programed into the machine to determine if the container is an acceptable returnable container for recycling under the Michigan Bottle Bill and

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<sup>3</sup> Appellant’s Brief in Docket No. 336871, Ex 1 Riegle Aff Tab A at ¶7; Ex 2 Tab A at ¶8.

<sup>4</sup> Appellant’s Brief in Docket No. 336871, Ex 4 Tab A at ¶¶9-10.

<sup>5</sup> Appellant’s Brief in Docket No. 336871, Ex 1 Riegle Aff Tab A ¶¶8-10; Ex 4 Riegle Dep at pp 17:24 to 18:10; p 22:7-11; p 30:20-24; and pp. 32:18 to 33:8.

<sup>6</sup> Appellant’s Brief in Docket No. 336871, Ex 1 Riegle Aff Tab A at ¶11; Ex 4 Riegle Dep at pp 30:24 to 31:2 and 32:21 to 33:8.

<sup>7</sup> Appellant’s Brief in Docket No. 336871, Ex 1 Riegle Aff Tab A at ¶12; Ex 4 Riegle Dep at p 16:11-17 and p 34:2-20.

<sup>8</sup> Appellant’s Brief in Docket No. 336871, Ex 1 Riegle Aff Tab at ¶¶13-14; Ex 4 Riegle Dep at p 22:3-11, and p 34:7-20.

the parameters of the TOMRA customer.<sup>9</sup> If a container is not an acceptable refundable container or is the incorrect material type, the container is rejected.<sup>10</sup> The Container Recycling Machine also uses the information from the UPC and the information programed into the machine to determine the material content of the container, the weight of the container, and the amount of material content along with the color of the content.<sup>11</sup> The Container Recycling Machine then attributes a raw material value to the container, as well as a deposit return value.<sup>12</sup> The Container Recycling Machine maintains a count of containers, their raw material value and deposit return value.<sup>13</sup> The containers are further sorted by material content into aluminum, plastic, and glass.<sup>14</sup> Aluminum cans are crushed and moved to an in-process bin within the Container Recycling Machine.<sup>15</sup> Plastic bottles are sorted by color and converted and conditioned by making waffle punctures and then compacted and moved to an in-process bin.<sup>16</sup> Glass containers are sorted by color: clear, green and amber, and moved to in-process bins.<sup>17</sup> The beverage containers are then transported to a processing plant where the beverage containers

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<sup>9</sup> Appellant's Brief in Docket No. 336871, Ex 1 Riegle Aff Tab A at ¶¶14-21; Ex 4 Riegle Dep at pp 19:3-10 to 20:25, p 22:3-11, pp 31:3-7, 31:22 to 32:17, and pp 33:19 to 34:1.

<sup>10</sup> Appellant's Brief in Docket No. 336871, Ex 1 Riegle Aff Tab A at ¶20; Ex 4, Riegle Dep at 19:11 to 20:5.

<sup>11</sup> Appellant's Brief in Docket No. 336871, Ex 1 Riegle Aff Tab A at ¶24; Ex 4 Riegle Dep at pp 21:20 to 22:11, 24:2-10, and p 34:2-20.

<sup>12</sup> Appellant's Brief in Docket No. 336871, Ex 1 Riegle Aff Tab A at ¶24.

<sup>13</sup> *Id.* at ¶¶23-24.

<sup>14</sup> *Id.* at ¶26.

<sup>15</sup> *Id.* at ¶28; Ex 4 Riegle Dep at p 22:7-11.

<sup>16</sup> Appellant's Brief in Docket No. 336871, Ex 1 Riegle Aff Tab A at ¶29; Ex 4 Riegle Dep at TOMRA000549, pp 35:18 to 36:17.

<sup>17</sup> Appellant's Brief in Docket No. 336871, Ex 1, Riegle Aff, at ¶5, Tab A at ¶31; Ex 4, Riegle Dep at pp 34:2 to 35:17.

are further processed, eventually being recycled into new containers, carpeting, automotive parts or other products.<sup>18</sup>

**B. TOMRA's Sales of Container Recycling Machines.**

During the tax periods at issue, TOMRA did not realize that the Container Recycling Machines were exempt under the industrial processing exemption and erroneously charged its customers Michigan sales tax on the sale or lease of Container Recycling Machines, as well as on the sales of parts and supplies for the Container Recycling Machines. The only items upon which TOMRA charged sales tax were the sales and leases of Container Recycling Machines and parts because services are not subject to tax. TOMRA remitted all sales tax to the Department.

For the tax periods at issue, TOMRA also remitted use tax to the Department on repair parts that were used by TOMRA to repair Container Recycling Machines in Michigan.

**C. The Audit and Claims for Refund.**

The Department conducted an audit of TOMRA for tax periods from 10/01/2003 through 12/31/2008. The Department issued an Intent to Assess Sales Taxes in the amount of \$516,562 plus negligence penalty of \$58,502 and interest of \$197,601.50. TOMRA submitted claims for refund to the Department for Michigan sales tax collected from TOMRA's customers and remitted to the Department. The Department denied TOMRA's refund for tax periods 10/01/2003 through 12/31/2008 and did not act on TOMRA's 2011 refund claim.

**D. Proceedings Before the Court of Claims.**

On October 17, 2016, TOMRA filed a Motion for Partial Summary Disposition and Declaratory Judgment in Docket No. 16-118-MT with the Court of Claims. After briefing by both parties, the Court of Claims granted Summary Disposition to the Department.

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<sup>18</sup> Appellant's Brief Docket No., Ex 1 Riegle Aff Tab A at ¶¶32 and ¶40; Ex 4 Riegle Dep at pp

Subsequently, the Court of Claims issued a Sua Sponte Order for filing of Briefs in Docket Nos. 14-91-MT and 14-185-MT. After briefing by both parties the Court of Claims granted Summary Disposition to the Department. In both cases, the Court of Claims held that regardless of whether the machines performed tasks that fit under subsection (3), they also perform raw material storage and are therefore not exempt.

**E. The Decision of the Court of Appeals.**

The Court of Appeals held that the definition of industrial processing under MCL 205.54t(7)(a) (“subsection (7(a))”) does not exclude specifically defined industrial activities under subsections MCL 205.54t(3) (“subsection (3)”) and MCL 205.54t(4) (“subsection (4)”). Under subsection (4) machinery used to perform an industrial processing activity is exempt. *Tomra of N Am, Inc v Dep’t of Treasury*, \_\_ Mich App \_\_, \_\_; \_\_ NW2d \_\_ (2018) (Docket Nos. 336871 and 337663); slip op. at 5. Subsection (7)(a) and (3) define industrial processing. Thus, activities that are plainly defined as industrial processing under these two subsections are exempt even if there is no raw material storage. The Court of Appeals refused to limit qualified industrial processing activities to only those activities immediately preceded by raw material storage. *Id.* at \_\_; slip op at 7. The Court of Appeals interpreted the reference to raw material storage as a delineation of when the non-exempt activity ended, rather than a precondition for the exemption just as this Court has determined that finished goods storage is not a necessary condition for the exemption in *Detroit Edison*. *Id.* at \_\_; slip op. at 7-8 n 5. Judge K.F. Kelly dissented. The case was remanded to determine the entitlement to the exemption.

### III. STATUTES AT ISSUE

The industrial processing exemption has existed for decades. The Legislature expanded the scope and reach of the industrial processing exemption in 1999 PA 117 by adding subsections that expanded and enlarged the controlling definition of “industrial processing” to apply to specific users, specific activities and specific equipment. See, e.g. Senate Legislative Analysis, SB 544, HB 4744, 4745, and 4586 (July 19, 1999) p. 4. The exemption was expanded to apply to sales of tangible personal property to persons who are not industrial processors if the tangible personal property is used to perform an industrial processing activity. MCL 205.54t(1)(c) and 205.94o(1)(c). Moreover, the Legislature added a general definition of industrial processing in subsection (7)(a) along with specifically identified activities that constitute industrial processing in subsection (3) and equipment that qualifies under subsection (4). MCL 205.54t(3), 205.54t(4), 205.94o(3) and 205.94o(4).

MCL 205.54t establishes an industrial processing exemption from the sales tax imposed upon the seller, and parallel sections under MCL 205.94o exempt from use tax for the consumer for, in relevant part:

*(1) The sale of tangible personal property to the following after March 30, 1999, subject to subsection (2), is exempt from the tax under this act:*

\* \* \*

*(b) A person, whether or not the person is an industrial processor, if the tangible personal property is intended for ultimate use in and is used in industrial processing by an industrial processor.*

*(c) A person, whether or not the person is an industrial processor, if the tangible personal property is used by that person to perform an industrial processing activity for or on behalf of an industrial processor.*

\* \* \*

(3) Industrial processing *includes* the following activities:

\* \* \*

(d) *Inspection, quality control, or testing to determine whether particular units of materials or products or processes conform to specified parameters at any time before materials or products first come to rest in finished goods inventory storage.*

\* \* \*

(g) *Remanufacturing.*

\* \* \*

(i) *Recycling of used materials for ultimate sale at retail or reuse.*

(j) *Production material handling.*

(k) *Storage of in-process materials.*

(4) Property that is eligible for an industrial processing exemption *includes* the following:

\* \* \*

(b) *Machinery, equipment, tools, dies, patterns, foundations for machinery or equipment, or other processing equipment used in an industrial processing activity and in their repair and maintenance.*

\* \* \*

(6) Industrial processing does not include the following activities:

(a) Purchasing, receiving, or storage of raw materials.

\* \* \*

(7) As used in this section:

(a) "Industrial processing" means the activity of converting or conditioning tangible personal property by changing the form, composition, quality, combination, or character of the property for ultimate sale at retail or for use in the manufacturing of a product to be ultimately sold at retail. Industrial processing begins when tangible personal property begins movement from raw materials storage to begin industrial processing and ends when finished goods first come to rest in finished goods inventory storage.



(b) “Industrial processor” means a person who performs the activity of converting or conditioning tangible personal property for ultimate sale at retail or use in the manufacturing of a product to be ultimately sold at retail.

\* \* \*

(d) “Remanufacturing” means the activity of overhauling, retrofitting, fabricating, or repairing a product or its component parts for ultimate sale at retail.

The Department must refund an overpayment of taxes unjustly assessed or wrongfully collected with interest. MCL 205.30(1).

Michigan’s Beverage Containers Act, 1976 IL 1, MCL 445.571 *et seq.* (hereinafter the “Bottle Bill”), requires beverage wholesalers, distributors, or bottlers to initiate a 10 cent deposit on returnable beverage containers and to transport returned used beverage containers from the retailers to processing centers.

#### IV. STANDARD OF REVIEW

##### A. Interpretation and Construction of Tax Statutes.

Clear and unambiguous language in a tax statute should be interpreted and enforced as written. *Ford Motor Co*, 496 Mich at 389. When tax imposition statutes are construed, however, any ambiguities are resolved in favor of the taxpayer. *Int’l Bus Machines v Dep’t of Treasury*, 220 Mich App 83, 86; 558 NW2d 456 (1996). Moreover, the Michigan Supreme Court has held that “tax collectors must be able to point to such express authority so that it may be read when it is questioned in court.” *In re Dodge Bros*, 241 Mich 665, 669; 217 NW 777 (1928).

Ambiguities in tax exemption statutes are construed against the taxpayer. *Guardian Indus Corp v Dep’t of Treasury*, 243 Mich App 244, 249; 621 NW2d 450 (2000); *Elias Bros Restaurants, Inc*, 452 Mich at 152. While a taxpayer has the burden of proof to show that it is

entitled to a tax exemption, a tax exemption should not be contracted or expanded by implication or a forced construction. *Ally Financial, Inc v State Treasurer*, \_\_ Mich \_\_; \_\_ NW2d \_\_ (2018) (Docket Nos. 154668, 154669 and 154670) (a strained construction of an exemption, contrary to Legislature's intent, is not permitted); *Mich Allied Dairy Ass'n v Auditor General*, 302 Mich 643, 650; 5 NW2d 516 (1942); *Mich Milk Producers, Ass'n v Dep't of Treasury*, 242 Mich App 486, 493; 618 NW2d 917 (2000); *Mich Bell Tel Co v Dep't of Treasury*, 229 Mich App 200, 208-210; 581 NW2d 770 (1998).

## V. ARGUMENT

### A. The Fundamental Principles of Statutory Interpretation Were Applied by the Court of Appeals and Review is Unnecessary.

The decision below faithfully adheres to the principles of statutory interpretation and creates precedent guiding other courts to observe statutory language. The Court of Appeals' repetition and application of foundational principles of statutory interpretation does not warrant this Court's review under MCR 7.305(B)(2), (3) and (5).

The principle rule for statutory construction is to discern and give effect to the Legislature's intent as expressed in the statutory language. *Massey v Mandell*, 462 Mich 375, 379-380; 614 NW2d 70 (2000); *DiBenedetto v West Shore Hosp*, 461 Mich 394, 402; 605 NW2d 300 (2000). "The Legislature is presumed to have intended the meaning it plainly expressed." *Linsell v Applied Handling, Inc*, 266 Mich App 1, 15; 697 NW2d 913 (2005). If the language is plain and unambiguous, then judicial construction is neither necessary nor permitted. *Guardian Photo, Inc v Dep't of Treasury*, 243 Mich App 270, 277; 621 NW2d 233 (2000).

**1. Under the Plain Language of the Statute, Activities Under Subsection (3) Are Industrial Processing Activities, Irrespective of Subsection (7)(a).**

The Department no longer challenges the determination that the Container Recycling Machines conduct activities (inspection, testing, quality control, sorting, crushing, shredding and recycling) that are identified as industrial processing activities under subsection (3). Rather, the Department takes issue with the Court of Appeals application of the two industrial processing definitions under subsections (7)(a) and (3) and failure to limit industrial processing to only those activities occurring after raw material storage. The Department's position is incorrect. First, under rules of statutory interpretation, a definitional section that identifies additional activities that are "included" in the primary definition is an expansion of that definition. Second, this Court has already recognized that industrial processing is defined under both subsections (7)(a) and (3). Finally, under this Court's *Detroit Edison* decision, neither raw material storage nor finished good storage is a necessary condition for industrial processing.

The court below correctly applied the statutory definitions of industrial processing under both subsections (7)(a) and (3). Subsection (7)(a) *defines* industrial processing as:

"Industrial processing" means the activity of converting or conditioning tangible personal property by changing the form, composition, quality, combination, or character of the property for ultimate sale at retail or for use in the manufacturing of a product to be ultimately sold at retail.

However, subsection (3) lists eleven categories of activities that are also defined as industrial processing by stating, "Industrial processing includes the following activities:." The court below noted that the question of whether the activities listed in subsection (3) are limited by the further statement in subsection (7)(a) that "Industrial processing begins when tangible personal property begins movement from raw materials storage to begin industrial processing and ends when finished goods first come to rest in finished goods inventory storage" requires construction of the

statute as a whole. *Tomra* at \_\_; slip op at 7. The court notes that the statute specifically defines what is and is not industrial processing and that all parts of the statute must be interpreted to give the words meaning and avoid a construction that would render any portion of the statute nugatory. *Id.* at \_\_; slip op at 6.

Subsection (3) activities are exempt without regard to subsection (7)(a). This conclusion is supported by the statutory construction principle that when a general definition in a statute conflicts with a specific modifier to that definition, the specific provision trumps the general definition. *Evanston YMCA Camp v State Tax Comm’n*, 369 Mich 1, 8; 118 NW2d 818 (1962). Moreover, where a term is defined by declaring what it “includes”, the definition is enlarged because “includes” is a term of enlargement, not restriction. *Mich Bell Tel Co v Dep’t of Treasury*, 445 Mich 470, 479; 518 NW2d 808 (1994), citing 2A Singer, Sutherland Statutory Construction (5<sup>th</sup> ed), § 47.07, pp 151-156. The Department previously agreed stating, “These modifiers [in subsection 3, 4, 5 & 6] demarcate the contours of ‘industrial processing’—regardless of whether the activity satisfies the definition of 54t(7)(a).” 2/18/2015 14-91-MT Department Motion for Summary Disposition, p 18. Now, the Department incorrectly argues that all activities under subsection (3) must also qualify under subsection 7(a) and occur after raw material storage to constitute exempt industrial processing. The Department argues the statutory phrase “industrial processing includes” in subsection (3) is not an expansion of the 7(a) definition. This is an error and is contrary to Michigan Supreme Court’s holdings. *NACG Leasing*, 495 Mich at 31.

The Department’s argument that exempt industrial processing activities must occur after raw material storage and before finished goods storage is contrary to the plain language of the statute. The court below correctly rejected the argument that subsection 7(a) limits exempt

industrial processing activities to only those activities that occur between raw material and finished goods storage because such an interpretation would render the foregoing provisions of the statute nugatory and is at odds with principles of statutory construction. *State Farm Fire & Cas Co*, 466 Mich at 146 (holding that courts must give effect to every word, phrase and clause in a statute and avoid an interpretation that would render any part of the statute surplusage or nugatory). Under the Michigan Supreme Court’s application of the general/specific rule of statutory interpretation, the Department’s assertion that all industrial processing activities must occur after raw material storage is incorrect.<sup>19</sup> Those activities specifically identified as exempt processing in subsection (3) must be excluded from any limitation for this subsection to have meaning as a definitional enlargement.

The court below properly determined that to limit the activities qualifying for industrial processing to only those activities that occurred after raw material storage would render portions of subsection (3) meaningless. Subsection (3) includes activities that occur wholly separate and apart from raw material storage and in some case prior to raw materials storage. For example, subsection (3) clearly exempts some activities that occur prior to raw materials storage or after finished goods storage, such as “research or experimental activities,”<sup>20</sup> “engineering related to industrial process,”<sup>21</sup> “planning . . . of production and other exempt activities,”<sup>22</sup> and “design . . . of production or other exempt machinery.”<sup>23</sup> Similarly, other activities defined by the Legislature as exempt industrial processing activities may occur without regard to raw materials storage,

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<sup>19</sup> *Mich Bell Tell Co*, 445 Mich at 479; 2A Singer, Sutherland Statutory Construction (7<sup>th</sup> ed), § 47.07, pp 310-312.

<sup>20</sup> MCL 205.54t(3)(b) and MCL 205.94o(3)(b).

<sup>21</sup> MCL 205.54t(3)(c) and MCL 205.94o(3)(c).

<sup>22</sup> MCL 205.54t(3)(e) and MCL 205.94o(3)(e).

<sup>23</sup> MCL 205.54t(3)(f) and MCL 205.94o(3)(f).

such as recycling<sup>24</sup> and “inspection, quality control, or testing.”<sup>25</sup> The Legislature plainly intended that all of the activities listed in subsection (3) would qualify as industrial processing activities and applying a limitation to those activities would improperly render portions of that subsection nugatory. Additionally, subsection 3(d) includes its own temporal parameter that does not restrict the start time or place for “inspection, quality control or testing...” as long as the activities occur prior to finished good storage. Subsection (3)(d) includes in industrial processing “[i]nspection, quality control, or testing to determine whether particular units of materials or products or processes conform to specified parameters *at any time before materials or products first come to rest in finished goods inventory storage.*” MCL 205.54t(3)(d) emphasis added. Only by interpreting the “raw material storage” limitation to be inapplicable, as the Court of Appeals did, does subsection (3) continue to have meaning as intended by the Legislature.

Moreover, this interpretation is in accord with this Court’s decision in *Detroit Edison*. In *Detroit Edison*, this Court was tasked with applying the industrial processing statute to the generation and transmission of electricity to determine what activities constituted industrial processing. This Court began by applying the definitions of industrial processing under both subsection (7)(a) and subsection (3). As the Court stated, “MCL 205.94o(7)(a) and MCL 205.94o(3) set forth the activity that does constitute ‘industrial processing.’” *Detroit Edison*, 498 Mich at 55; and

“[i]ndustrial processing” activity is generally defined by MCL 205.94o(7)(a). However, the statute also provides that certain specific activities that do not satisfy the general MCL 205.94o(7)(a) definition nonetheless constitute “industrial

<sup>24</sup> MCL 205.54t(3)(i) and MCL 205.94o(3)(i).

<sup>25</sup> MCL 205.54t(3)(d) and MCL 205.94o(3)(d). Logically, raw material testing occurs before use in production for quality control. Testing raw materials is exempt and equipment used to test raw materials and for quality control function are exempt. Revenue Admin Bull 2000-4 Example 4.

processing” activity for purposes of the statute. [*Detroit Edison*, 498 Mich at 49 n 13.]

See also *Id.* at 48 n 12 stating that inspection, quality control or testing are industrial processing; and *Id.* at 54 n 19 disagreeing with the dissent’s position that industrial processing activity occurring outside a factory is a taxable activity. Thus, this Court has recognized that the industrial processing activities in subsection (3) are an expansion of the definition in subsection (7)(a) and the court below adhered to that holding.

The Department implies that subsection (3) is not part of the analysis by incompletely quoting this Court’s *Detroit Edison* opinion as setting forth a test looking only to subsection (7)(a).<sup>26</sup> This Court actually stated that the test for industrial processing is to determine whether industrial processing activity is occurring under either MCL 205.94o(7)(a) or MCL 205.94o(3).<sup>27</sup>

## **2. The Court of Appeals Properly Held that the Container Recycling Machines Qualify for the Industrial Processing Exemption.**

In this case the Department made various arguments for why the Container Recycling Machines at issue do not qualify for the industrial processing exemption under the statute, including: the machine owners are not industrial processors; the machines conduct only raw material storage; the exclusion for raw material storage trumps the application of the exemption to otherwise qualifying activities under subsection (3) and, now, that qualifying industrial processing activities are disqualified because they are not identified as occurring as part of the movement from raw material storage. All of the Department’s arguments have been overruled or abandoned by the Department. The Court of Appeals faithfully followed this Court’s holding that “[T]o determine whether the industrial processing exemption applies, it is necessary to consider the *activity* in which the equipment is engaged and not the *character* of the equipment-

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<sup>26</sup> Department of Treasury’s Application for Leave to Appeal (“Dep’t App”) at 10.

owner's business." *Elias Bros Restaurants, Inc*, 452 Mich at 157 (emphasis added). Under MCL 205.54t(4)(b), if the machines conduct an industrial process they are exempt. The only issue before the Court of Appeals was whether the activities of receiving, sorting, inspecting, performing quality control, performing production material handling, crushing, shredding and recycling beverage containers constituted industrial processing as a matter of law. The court below properly found that these activities qualify under the plain language of the statute and this Court's precedential decisions.

The Department argued that the raw material storage exclusion trumps the specific exemptions in subsection (3) for other activities because "when a specified 'exclusion' applies, it will take the activity outside the exemption" citing *Granger Land Dev Co.*<sup>28</sup> However, this holding was rejected by the *Detroit Edison* opinion and only cited by the dissent<sup>29</sup>. The majority stated:

[T]he activities enumerated in MCL 205.94o(6)(b) are not "specific modifier[s]" to the "general definition" of industrial processing set forth in MCL 205.94o(7)(a), as defendant suggests. Rather, MCL 205.94o(6) sets forth those activities that do not constitute "industrial processing," and MCL 205.94o(7)(a) and MCL 205.94o(3) set forth the activity that does constitute "industrial processing." [*Detroit Edison*, 498 Mich at 55 (opinion of the Court)].

In *Detroit Edison*, this Court clarified, "the nonexempt activities in MCL 205.94o(6)(b) are in no way within the scope of MCL 205.94o(7)(a), and the exempt activity in MCL 205.94o(7)(a) is in no way within the scope of MCL 205.94o(6)(b)." *Id.* at 45. Thus, under *Detroit Edison*, because the Container Recycling Machines activities of recycling, inspection, testing, quality

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<sup>27</sup> *Detroit Edison*, 498 Mich at 39.

<sup>28</sup> *Granger Land Dev Co v Dep't of Treasury*, 286 Mich App 601; 780 NW2d 611 (2009).

<sup>29</sup> *Detroit Edison*, 498 Mich at 63 (Kelly, J., dissenting).



control and remanufacturing are industrial processing activities under subsection (3) and the sorting, crushing and puncturing change the composition, form, quality and combination of the property under subsection (7)(a), they do not fall under any exclusion of MCL 205.54t(6) (“subsection (6)”) because activities qualifying under subsection either 7(a) or (3) are not within subsection (6). *Id.*

The Department argues that any in-machine storage must be “raw material storage” and anything that comes before it is disqualified, nonexempt activities. However, when storage occurs *after* the processing activities specifically identified under subsection (7)(a) and (3), such storage is exempt storage of in-process materials under subsection (3)(k). There is no storage of raw, unprocessed, untested, unsorted, uncrushed or nonpunctured bottles and cans in the Container Recycling Machines. Court of Claims’ conclusion that “regardless of whether Plaintiff’s recycling machines perform tasks that might fit within any specific provision of MCL 205.54t(3) or MCL 205.94o(3), because those activities occur before the industrial process begins, the exemptions . . . do not apply” is directly contrary to *Detroit Edison* and must be reversed.

**B. Failure to Perform a Non-Exempt Activity Does not Disqualify an Activity From Industrial Processing.**

Raw material storage is not a prerequisite for exempt industrial processing activity. The start of industrial processing is delineated, not by raw material storage, but rather *movement of the raw material to processing activity* or by processing activity. MCL 205.54t(7)(a). The Department argues for reading in a requirement that raw material storage occur first before any activity, even those defined by statute, can qualify as industrial processing. This improperly reads into the statute a limitation not imposed by the Legislature. Moreover, as the Court of Appeals noted, the requirement sought to be imposed is nonsensical because TOMRA would

qualify for the exemption if it merely required consumers to first put used beverage containers into a bin before putting them into the Container Recycling Machines even though the Container Recycling Machine's activities would be unchanged. *Tomra*, \_\_ Mich App at \_\_; slip op at 5 n 3.

The Court recently opined on the scope of the industrial processing exemption in *Detroit Edison*, 498 Mich 28. The Court specifically addressed two key issues regarding the industrial processing exemption: (1) how the delineation of the beginning and end of industrial processing added to MCL 205.94o(7)(a)<sup>30</sup> should be interpreted; and (2) whether a specific exclusion from industrial processing under MCL 205.94o(6) trumps a specific inclusion for activities within industrial processing. Under *Detroit Edison*, neither raw material storage nor finished good storage is required for exempt industrial processing to occur. In *Detroit Edison*, all parties agreed that electricity processing activity occurred (as defined under the first sentence of MCL 205.94o(7)(a)) at a generating plant and the Court found that processing also occurred under MCL 205.94o(3). *Id.* at 38. However, the Court found that there was no evidence establishing the point at which the electricity at issue came to rest in finished goods inventory storage. *Id.* at 41. Accordingly, the Court looked to when the processing was completed as the end of industrial processing. Systematically, the Court of Appeals look to when processing began by looking at the start of activity defined as industrial processing. Moreover, as discussed below, the *Detroit Edison* Court held that concurrent non-industrial processing activities do not negate the application of the exemption to activities defined as industrial processing under MCL 205.94o(7)(a) and (3). *Id.*

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<sup>30</sup> The provisions of MCL 205.94o, which contains the industrial processing exemption from use tax, and MCL 205.54t, which contains the industrial processing exemption from sales tax, are identical.

Just as there is no requirement for finished goods inventory storage to complete industrial processing, there is no requirement that there be raw materials storage prior to industrial processing. Many manufacturers use “Just in Time Manufacturing,” in which there is no raw material storage.<sup>31</sup> Rather, raw material inventory is delivered as it is needed for processing and production.<sup>32</sup> The Department recognizes the use of Just in Time Manufacturing and exempts the movement of raw material “whether it goes directly to the production machinery or to a staging area near the production process.”<sup>33</sup> The Department’s own Industrial Processing Training Manual recognizes that delivery of raw materials to a machine that processes the materials is exempt even in the absence of raw materials storage.<sup>34</sup> Indeed, in Example 4 therein, parts are unloaded onto an exempt conveyer to the production area, without any storage. *Id.* (“In this example, there is no taxable material handling area activity as the movement of the purchased parts is to the production area, being driven by the production process.”).

In this case, the introduction of the beverage container into the Container Recycling Machine is a just-in-time process. Empty beverage containers are collected by consumers and often gathered by individuals from waste receptacles or the ground.<sup>35</sup> Introduction of the beverage container into a Container Recycling Machine delivers the container to the start of processing and triggers movement away from raw material storage (a waste receptacle or

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<sup>31</sup> See Hunt, The “Just-In-Time-Method” <<http://smallbusiness.chron.com/justintime-method-31185.html>> (accessed March 13, 2017).

<sup>32</sup> *Id.*

<sup>33</sup> Appellant’s Brief in Docket No. 336871, Ex 11 excerpt from Michigan Department of Treasury - *Revenue Technical Tax Training, Sales and Use Tax: The Industrial Processing Exemption*, July 2002.

<sup>34</sup> *Id.* Ex 11.

<sup>35</sup> The Beverage container law was enacted to prevent litter and require container recycling. MCL 445.571 to 445.576.

shopping cart) to performance of inspection, quality control, testing, sorting (MCL 205.54t(3)(d)), remanufacturing (MCL 205.54t(3)(g)), production material handling (MCL 205.54t(3)(j)), recycling activities (MCL 205.54t(3)(i)) and storage of in-process materials (MCL 205.54t(3)(k)). In fact, the Container Recycling Machines at issue are required by law to perform the exempt processing activities of testing, quality control and sorting under the Reverse Vending Machine AntiFraud Act, 2008 PA 387.<sup>36</sup>

The requirement that there be “raw material storage” prior to industrial processing is at odds with the Legislature’s definition of “remanufacturing” and “recycling” as industrial processing activities because remanufacturing and recycling activities do not begin with raw materials but instead begin with a finished product. Indeed, the Court of Claims requirement essentially renders these sections of the industrial processing exemption nugatory. One way to avoid this conflict is to recognize that a product that is being recycled or remanufactured, such as a beverage container, started its movement from raw material storage when it was first manufactured and remanufacturing or recycling is therefore always occurring after raw material storage. Another way to avoid the conflict in this case is to note that, even if there was a requirement for raw material storage, there is no requirement as to who is required to perform it. Therefore, the shopping cart or shopping bag that consumers use to store used beverage containers would qualify as raw material storage and insertion of the container onto the Container Recycling Machines conveyer belt is the first movement from raw material storage.

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<sup>36</sup> 2008 PA 387 requires the Container Recycling Machines to contain vision technology to perform the quality control, testing and sorting processes. MCL 445.653(t) defines a “reverse vending machine” as a device to identify and process empty containers.

### C. Recycling is an Industrial Processing Activity.

The Department misconstrues the bottle and can recycling process. MCL 205.54t(3)(i) states that “recycling” of used materials is an industrial processing activity. Recycling is not defined by the statute, but is defined in the dictionary<sup>37</sup> as “to process (something, such as liquid body waste, glass, or cans) in order to regain material for human use.” Merriam-Webster Online.<sup>38</sup> Recycling is an activity that occurs in stages, often with each stage conducted by separate persons, but for which all stages are necessary to reprocess waste into a new product for sale to consumers. Production from recycled materials requires uncontaminated bottles and cans separated by material into aluminum, plastic and glass with plastic further separated by grade and color and glass further separated by color. Inspection and sorting the waste stream is the start of the industrial process of recycling.<sup>39</sup>

The Container Recycling Machines begin the process of recycling bottles and cans by conducting the first steps of recycling through not only inspecting and testing an offered bottle or can but also by quality control, sorting by material, grade and color and crushing or puncturing of accepted containers followed by in-process storage. Material sorting by composition, grade and color is an essential part of recycling so that pure inputs are converted into the new product.

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<sup>37</sup> In the absence of contrary direction by the Legislature, words used in a statute are to be given their ordinary meaning. *Sanchick v State Bd of Optometry*, 342 Mich 555, 559; 70 NW2d 757 (1955). (“Words will be given their usual and customary meanings, save as otherwise defined. ...” [Emphasis added.] )

<sup>38</sup> Recycling definition <<https://www.merriam-webster.com/dictionary/recycling>> (accessed August 7, 2017).

<sup>39</sup> Sorting and compression is the first step in aluminum recycling. Process of Aluminum Recycling <<http://www.conserve-energy-future.com/aluminum-recycling.php>> (accessed August 10, 2017). Sorting glass by color is the first step for recycling. See The Glass Recycling Process <<http://www.all-recycling-facts.com/glass-recycle.html>> (accessed August 10, 2017) and Glass Recycling <<http://www.conserve-energy-future.com/recyclingglass.php>> (accessed August 10, 2017). Sorting by resin content and color is the first step in plastic bottle recycling <<http://www.conserve-energy-future.com/recyclingplastic.php>> (accessed August 10, 2017).

The machines at issue conduct recycling processing and are entitled to the industrial processing exemption as a matter of law.

Moreover, the “inspection, quality control, or testing to determine whether particular units of materials or products or processes conform to specified parameters” is exempt if performed “*at any time before materials or products first come to rest in finished goods inventory storage*” under the plain language of subsection (3)(d). The Department confirms exemption of pre-storage testing in Revenue Admin Bull 2000-4, stating:

Example 5 An industrial processor performs tests on its raw materials. The equipment and supplies used for or consumed by an industrial processor in this testing and quality control function are exempt.

The statute only requires exempt testing activity be conducted *prior to finished good storage*.

The Container Recycling Machines fall directly under the plain language of the statute and the RAB’s interpretation and application of the statute.

**D. The Decision has Minimal Impact.**

The Department urges this Court to grant leave because the decision is “a judicially created tax loophole that will result in the loss of millions of dollars.” Dept Application at 2. A Legislatively granted exemption is not a loophole and the Department itself states that “this case alone concerns approximately \$700,000.” Dept Application at 14. This is hardly millions. The purported additional exemptions for cardboard and paper shredders simply will not materialize because all exemptions have to be by or for an industrial processing for manufacture of a product for resale. A grocery store shredding paper will not qualify for the exemption unless shredding is part of a recycling process that results in manufacture of a product for resale. In this case, the record is replete with evidence that the beverage containers at issue were recycled into new

products for sale. The record contains uncontroverted testimony by Charles W. Reigle, TOMRA Sr. Vice President of Government Affairs that:

- The crushed aluminum cans were delivered to Novelis, Alcoa, and Coca-Cola recycling for manufacturing into new containers; Reigle Dep 28:23 – 29:15.
- The punctured and color and grade sorted plastics were sold to a variety of plastic reclaimers who converted them for use to manufacture bottles, carpeting, automobile parts and other higher end uses; Reigle Dep 47:10 – 48:13.
- The color sorted glass containers are ultimately delivered to Owens Illinois and Verailia for manufacturing into new glass containers. *Id*; See also Reigle Aff at ¶32.

The whole purpose of Michigan's mandated deposit law is to put the bottles and cans into the recycling process.<sup>40</sup> Unlike any hypothetical machines and exemption claims, there is no real dispute that the aluminum, plastic and glass containers that begin recycling in the Container Recycling Machines are ultimately used by industrial processors for manufacture into products for sale at retail as required by MCL 205.54t and 205.94o. If other taxpayers can produce the same proofs, they will be entitled to the exemption. However, there is no evidence in the record that the Department will be inundated by such claims.

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<sup>40</sup> National Conference of State Legislators, State Bottle Deposit Laws <<http://www.ncsl.org/research/environment-and-natural-resources/state-beverage-container-laws.aspx>> (accessed 8/10/2017).

**VI. CONCLUSION**

The Court of Appeals decision below is a routine application of the well-established rules of statutory construction that confirms to this Court's prior precedential cases for statutory interpretation. The Court should deny the Application for Leave to Appeal.

Respectfully submitted,

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Dated: September 25, 2018

By: /s/ June Summers Haas  
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